

Service Date: March 22, 1984

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER of the Application)	UTILITY DIVISION
by THE MONTANA POWER COMPANY for)	
Authority to Increase Rates for)	DOCKET NO. 83.9.67
Electric Service.)	INTERIM ORDER NO. 5051

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FINDINGS OF FACT

1. On September 30, 1983, the Montana Power Company (Applicant or MPC) filed an application with this Commission to increase rates by \$96,367,013.
2. On February 3, 1984, Applicant filed an application for interim rate relief in the amount of \$81,305,068. The Applicant proposed an alternative interim request which sought to increase rates immediately by \$42,281,810. The remaining \$39,023,258 was to be accumulated for disposition as a surcharge in a final order in this docket.
3. Pursuant to the Commission's rules on interim rate increases, ARM Sections 38.5.501, et seq., Applicant has given proper notice of its interim rate increase request.
4. Comments in opposition to an interim rate increase were received from Anaconda Minerals Company, Exxon, Stauffer Chemical Company, Montana Irrigators, Inc., Champion International, Conoco, Northern Plains Resource Council, and District XI Human Resource Council. The comments in opposition raised these points: (1) the large impact of MPC's interim rate request on ratepayers' bills; (2) the contested nature of costs associated with Colstrip #3 and related facilities; and (3) that no interim rate request should be granted prior to a public hearing.
5. On March 1, 1984, MPC filed a response to the above-listed intervenors' objections to interim relief. In its response, MPC's main contention was that failure of the Commission to grant interim rate relief would result in serious and irreparable harm to the MPC electric utility.

COMMISSION DISCUSSION AND ANALYSIS

6. This application is the largest rate increase request ever filed in the State of Montana. It is not surprising, in view of that fact, that it is the most contested one, at least in recent times. Over 20 parties have intervened; media coverage has been intense; correspondence to the Commission from the general public is voluminous. Similarly, in keeping with the magnitude of the case, MPC's filing is the most voluminous ever received by the Commission for an electric rate increase request.

7. In keeping with the unprecedented size of the case, MPC's interim filing is also unusual. Both the Commission's rules on the matter and recent utility practice anticipate the Commission's review of an interim increase application soon after the filing of the case in chief. In this case, however, MPC filed its interim request four months after its general filing and almost a full month after the Colstrip 3 plant went into commercial operation.

8. This delay resulted in the interim request being filed just shortly before intervenors' testimony was filed. This situation is similar to the Commission's general practice prior to adoption of its rules governing interim increase requests. Prior to the rules, the Commission granted interim increases only after intervenor testimony was filed. This practice gave customers and the Commission some assurance that the interim increase would not be higher than the rates approved in a final order. This practice was abandoned for at least two reasons: 1) The Montana Consumer Counsel believed that its testimony was being incorrectly used; 2) in the recent years of double digit inflation the utilities argued that delays inherent in the process resulted in unacceptable attrition in their earnings.

9. Because of these arguments, the Commission adopted and then amended its interim rules. The rules, as they stand today, attempt to strike a balance between speedy rate relief and increases that include generally accepted items not likely to be contested by other parties. For example, the cost of equity used to determine interim rate levels are those found appropriate in the previous general rate case. (Arm 38.5.506(1)(b).) Similarly, new expense items must be "clearly identifiable." (ARM 38.5.506(3)(a).) The philosophy reflected by the interim rules has often been described as a "make whole" approach. In other words, the rules contemplate that a utility's rates be updated to reflect current economic realities while avoiding rates that may reflect controversial contested claims. This approach was adopted to address the utilities' desire for speedy rate relief

while anticipating by rule, areas of potential conflict that require full airing in a hearing. Perhaps the prime example of this approach is the use of a previously determined cost of equity, since this is a perennially contested issue.

10. One other underlying philosophy of the interim rules should also be mentioned. Because the rules contemplate increases prior to intervenor testimony, they were designed to allow the Commission and its staff to quickly determine, basically as an accounting matter, a reasonable increase for utilities. They were intended to avoid, to the extent possible, prejudgment of contested and complex issues, while assuring some rate relief to the utility.

11. The specific issue of how interim rate increases should reflect substantial additions of new plant investment is not specifically addressed in the Commission's interim rules. This omission is not unusual in view of the rules' intent to provide an updating of expenses found reasonable in the previous rate case, expenses such as wages, taxes and other objectively identifiable items.

12. This "update"/"make whole" philosophy cannot serve as grounds for allowing a major new plant addition prior to a thorough exploration of the underlying issues associated with it. This is especially so, given the fact, as in this case, that the addition of that substantial new investment to MPC's rate base, is now one of the most contested issues in this , proceeding.

13. Certainly, as MPC asserts, the expenses associated with operation of Colstrip 3, may be determined to some extent. At least, the Commission, from prior experience, can assume that there are expenses associated with the operation of so large a plant. Unanswered, however, are major legal and factual issues. Before plant investment can be included in the rate base upon which it is allowed the opportunity to earn a profit, it must be found "used and useful by the Commission." (69-3-109, MCA). In this case, the Commission takes note that prefiled testimony and motions have discussed the issue. On the one hand, MPC's filing claims 1) Colstrip 3 is used and useful; 2) the Commission is

prohibited from reviewing the issue in view of the Board of Natural Resources and Conservation's determination that Colstrip 3 and 4 are "needed," pursuant to the Montana Major Facility Siting Act. (75-20-101, et seq., MCA). On the other side of the issue stand Intervenors' prefiled testimony

containing a panoply of recommendations, which provide a number of alternatives to MPC's request for full rate base treatment.

14. Given the status of the issue regarding treatment of this Colstrip 3 plant, it is impossible for the Commission to conclude, at this stage of the proceeding, that rate base treatment, with all of the associated revenue items, merely constitutes an updating of previous expenses, as is contemplated by the interim rules.

15. Nonetheless, the interim rules do provide some guidance in the matter. ARM 38.5.506(1) states: "Consideration of an application to increase rates on an interim basis in a general rate increase proceeding will be guided by generally established principles of utility rate regulation." One of those principles is that contested issues should be thoroughly aired before customers pay for a utility's investment decisions. Long before the modern development of detailed requirements for administrative proceedings, public service commission proceedings were subject to extensive due process requirements, including rules of evidence, the right to cross-examine and the right to be heard. In Montana, those rights were attenuated by the statute that allowed increases prior to hearing. 69-3-304, MCA. But, importantly, that law left immediate increases to the Commission's sound discretion.

16. MPC's Response to Intervenor Objections to Applicant's Motion for Interim Rate Increase (Response) raises several issues that are appropriate to address in preliminary fashion at this time.

The first of those issues is the claim that MPC is currently incurring costs because of Colstrip 3. As previously mentioned, the Commission does not disagree with that assertion (although the levels may be disputed). Contrary to MPC's assertions however, is the basic requirement that only prudent expenses may be reflected in rates. Whether expenses are prudent, if associated with a plant that may not be used and useful, is a contested issue in this case.

17. MPC also argues that, "Upon commercial operation, the company may no longer capitalize an allowance (sic) for funds used during construction (AFUDC)." By separate order issued simultaneously with this order, the Commission has negated this claim. That order specifically allows an interest allowance on the capital costs associated with Colstrip 3 from the date of commercial operation. This treatment assures that MPC will be compensated for capital costs

associated with Colstrip 3 (though on a delayed basis), assuming that MPC prevails in its arguments that all Colstrip 3-related investment should be included in rate base. Contrary to MPC's argument (Response, p. 11) by this order, the PSC has addressed the possibility that delay would leave MPC with "no remedy whatsoever." Thus, by this order, MPC will suffer no permanent loss of revenue that it is entitled to receive.

18. Similarly, MPC argues that a day's delay is a day's loss of deserved revenues. As previously noted, MPC itself delayed filing its interim request until almost one month after Colstrip 3 went into commercial operation. MPC thus seems to argue implicitly that its own delay will not harm the company, but that Commission-caused delay will have the opposite effect. In this context, the Commission wishes to address the delay between the date MPC filed its interim request and the date of this order. As previously noted, MPC spent between September 30, 1983 and February 3, 1984, formulating its interim request. By contrast, the PSC has taken from February 3, 1984 to March 20, 1984 to analyze the request. This time has been used in analyzing the request (two different levels), as well as considering Intervenor Objections and MPC's Response. (MPC requested that a decision on the interim request be delayed until March 1, so that it could respond to objections.) In addition, the Commission staff spent a considerable amount of time discussing its analysis with company personnel.

19. In its Response, MPC places substantial reliance on Montana law's provision for rebate (69-3-304, MCA), should interim rates be higher than those found reasonable in the PSC's final order. The Commission agrees with MPC to the degree that the rebate provisions provide some protection to MPC's consumers for interim rates that are found artificially high in a final order. The Commission disagrees, however, with the suggestion that, because of rebate provisions, it should be indifferent to interim rate levels. Total reliance on rebates ignores several important issues: 1) If the Commission finds rebates appropriate, it also finds implicitly that MPC customers have been loaning the company funds. In effect, the Commission's order has converted customers into lenders. As a rule, rates should, to the extent possible, not include involuntary loans. 2) Some customers who have paid the interim rates will leave the system at the time rebates are ordered. 3) Even for those who remain on the system during the time of interim rates and the rebate period, it is often a difficult task to assure that, individually, each customer will receive the rebate due, given consumption during

the interim rate period as opposed to the rebate period. Rebates, contrary to MPC's argument, provide at best, an incomplete solution to interim rates that are adjusted downward in a final order.

It is worth noting that MPC and other utilities made precisely the same arguments to the Legislature in 1981 when they urged adoption of Senate Bill 301, which would have allowed rate increases to go into effect as soon as a case was filed with the Commission. Full rebates would have been provided if the Commission later cut back the request. The defeat of SB 301 might reasonably be interpreted as the Legislature's rejection of the utilities' arguments that rebates provide the answer to quick large increases that are later scaled back.

20. MPC's Response highlights the possibly "staggering" effects of denial of interim rate relief. (Response p. 4, 1. 3) Although the Commission must certainly consider the possible effects of a denial or partial denial, it must balance those against those of MPC's consumers. The Commission does not believe that any party, including MPC, discounts the "rate shock" effects on consumers, whether they be residential, commercial, irrigation, industrial, or any other class, if they are to pay rates that reflect the request in this proposal. It is interesting to note, however, that while MPC describes the effect of a denial of interim relief in Draconian terms, it dismisses the effect of a grant on its customers as a "short term inconvenience." (Response, p. 11) Information presently before the Commission does not allow such a conclusion, at least at this time. Northern Plains Resource Council's discussion of the effect on irrigators is relevant to this point. (Objection, p. 2) See also District XI Human Resource Council's Objection, p. 2.

21. MPC's Response argues vigorously that Montana's laws provide for interim increases even if a particular issue is contested. The Commission agrees with the assertion, as far as it goes. Ignored in MPC's analysis, however, is that the law, while allowing for interim rate relief, does not require it. Rather, the statute allows the Commission, in its sound discretion, to approve, deny, or approve in part, such requests. Were MPC's interpretation to be accepted, those rates should become effective on the date selected by the utility to file its permanent request, as was contemplated by SB 301.

22. In its Response, MPC attached an Affidavit sponsored by Frank V. Woy, Executive Vice President, Finance, for MPC. Mr. Woy's statement includes an analysis of the effects of denial of the requested interim increase. The analysis is flawed in several respects. Most importantly, Mr.

Woy's analysis projects the effect of denial of the interim into the years of 1985 and 1986. However, at most, the interim increase will affect rates for a maximum of four months. Therefore, even Mr. Woy's projections for 1984 are misleading. Final rates, due at the end of July, 1984, will determine MPC's income for the balance of 1984. If a decision is not rendered in July, 1984, MPC may put into effect the full increase it has requested. (69-3-302(2), MCA) As previously mentioned, MPC itself choose, by the timing of its interim filing, to forgo potential revenues associated with Colstrip 3 between the time of its commercial operation (January 10, 1984) and the date of its Response to objections to the request (March 1, 1984). In addition, the Commission fails to see the relevance of Mr. Woy's analysis that covers the years of 1978 through 1983 in view of the previous discussion.

23. Many of the Intervenor's objections suggest that the Commission should grant absolutely no rate relief on an interim basis. However, an examination of arguments in support of the objections suggest that they are directed primarily to reflecting Colstrip-related expenses in interim rates. The level of increases found appropriate in this order seem to address the major concerns of objections filed.

24. Some Intervenor's objections claim that an interim increase cannot be granted prior to a formal hearing. This position is directly contradicted by the interim statute, Section 69-3-304, MCA, and the Commission specifically rejected this position when it promulgated the interim rules.

25. Based on the information presently filed in this proceeding, the Commission finds that partial grant of MPC's interim rate increase request is appropriate. The grant reflects the letter, spirit and philosophy of the Commission's rules, under which MPC and all other utilities have functioned for several years.

26. The increase found appropriate excludes claimed costs associated with Colstrip 3. The Commission interprets this exclusion as being consistent with the interim rules and past Commission practice. See Docket No. 81.8.70, Interim Order No. 4881, Finding of Fact No. 7.

27. Because of the importance of this case and the significant financial stakes for all involved, the Commission reserves the right to adjust the rate levels found appropriate in this order, as evidence in the case develops, and prior to the final order.

28. With the elimination of Colstrip No. 3, adjustments to MPC's resource mix are necessary for this Interim Order. In the MPC resource mix, output from the Corette Plant was

reduced in the months of February, March, July and August to allow for increases in opportunity purchases. The Commission raised the output from Corette to 136 MW in each of these months to reflect the normal energy capability of that plant. The 32 MW output from Corette in April (the month in which maintenance is performed) filed by MPC is accepted by the Commission. In Docket No. 82.8.54, MPC proposed that opportunity purchases be included in the resource mix at 22 MW per month except for the months of May and June. Montana Consumer Counsel witness George Hess felt that that level was too low in comparison with recent experience. He noted that in 1980 MPC's opportunity purchases amounted to 85 average megawatts; in 1981, opportunity purchases were 100 average megawatts; and for the first 11 months of 1982, opportunity purchases were 138 average megawatts. Hess did not agree with the price of 20 mills for opportunity purchases filed by MPC. Based again upon recent experience, Hess recommended a price of 17 mills for opportunity purchases. In Docket No. 82.8.54, Order No. 4938a the Commission found that opportunity purchases should be included at the level of 50 MW per month except for the months of May and June, when the numbers filed by the Applicant were accepted. The Commission found the price of opportunity purchases to be 18 mills based upon actual experience for 1980 and 1981. Until these issues can be fully examined at the hearing in this Docket, the Commission finds these adjustments to be appropriate for the calculation of interim relief.

29. The Commission reversed an adjustment made by MPC which eliminated revenues received from Puget Sound Power and Light for the use of transmission facilities. The revenues from Puget are payments for use of the transmission system of MPC for Colstrip 1 and 2. Recognition of these revenues is necessary to reflect the transmission system which existed prior to Colstrip 3. This adjustment by the Commission increased revenues by \$3,777,910.

30. The Commission finds that, contrary to the Company's filing, the Hanford contract should remain as part of MPC's resource mix for purposes of determining the appropriate interim increase in this case. This determination is based on the approach, adopted in the interim rules, that certain items should remain as they were in the previous final rate order until a final determination can be made in the current Docket. This approach is preferred over the known and measurable change approach in this instance, because parallel items have not been updated from the last case, although they too have changed. Most noteworthy of these is the opportunity purchase level and

price and the off-system sales price. Although the prices and sales levels have changed since the last rate case, for purposes of the interim request, the price and sales levels determined in the last MPC rate case were used. To change some items and not others would result in a mismatch that would distort the snapshot that any interim rate determination necessarily indicates.

In addition to the mismatch problem, the Commission notes that MPC's decision not to renew the Hanford contract is a contested issue in this case, as is the more general area of load and resource match. See, for example, Docket No. 83.9.67 prefiled testimony of John Duffield, p. 13.

31. Replacing the Hanford contract as a resource results in an increase in purchased power expense of \$5,446,678. This adjustment has the effect of increasing the amount of out-of-state sales by 459 MW. Out-of-state sales are increased \$9,245,874 as a result. Therefore, the adjustment results in a \$3,799,196 decrease.

32. Coal costs were revised by MPC in its interim filing to reflect a change in freight cost and a change in coal cost adjustment factors. The Commission accepts this adjustment for the purpose of determining interim relief. Consistent with past practice the Commission prefers the use of updated actual data to estimates.

33. As a result of the adjustments made by the Commission, revenue for interim purposes are \$224,494,938, and the total cost of service is found to be \$170,773,900. This results in a balance for return of \$53,721,038.

34. The Applicant's required interim relief in the amount of \$3,859,009 is determined as follows:

Electric Utility Rate Base	\$480,029,053
Interim Rate of Return	<u>11.61%</u>
Required Return	\$ 55,731,373
Balance for Return	<u>53,721,038</u>
Income Deficiency	\$ 2,010,335
Tax Multiplier	<u>.5030</u>
Revenue Deficiency	\$ 3,996,689
Less: REC Revenue Deficiency	<u>137,680</u>
Interim Revenue Increase	<u>\$ 3,859,009</u>

CONCLUSIONS OF LAW

1. The foregoing findings of fact are hereby incorporated as conclusions of law.

2. The Montana Power Company is a public utility furnishing electric service to consumers in the State of Montana. As such, it is subject to the supervision, regulation, and control of this Commission, Section 69-3-102, MCA.

3. Section 69-3-304, MCA, provides in part, "The Commission may in its discretion temporarily approve increases pending a hearing of final decision." Contrary to the arguments contained in MPC's Response, this provision does not give it a right to immediate rate relief. Montana law generally contemplates that whatever rate relief is found appropriate by the Commission is to be granted within nine months of the date of filings. 69-3-302, MCA

4. The amount of interim relief approved in this order meets the requirements of the rules governing interim increases, ARM 38.5.501 et seq.

5. Because of the accounting treatment allowed in Order No. 5051a, the decision in State v. Public Service Commission, 169 Mont. 99, 548 P.2d 136 (1976) is not applicable to the Commission's decision in this proceeding.

ORDER

1. The Montana Power Company is hereby GRANTED authority to implement, on an interim basis, increased electric rates designed to generate \$3,859,009, in additional revenues on an annual basis.

2. The Montana Power Company is to file revised rate schedules reflecting a uniform percentage increase applied to all rates resulting from the interim revenue increase granted herein.

3. Nothing in this Interim Order precludes the Commission from adopting in its final order, after reviewing the entire record in this docket, a revenue requirement different from that contained in this order.

4. The interim relief granted in this order is to be effective for electric service rendered on and after March 21, 1984.

5. Interim revenues granted herein are subject to rebate should the final order in this docket disapprove this interim revenue increase. Such a rebate would include interest at the currently authorized rate of return on equity (14.14 percent).

DONE IN OPEN SESSION at Helena, Montana, this 20th day of March, 1984, by a vote of
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BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

THOMAS J. SCHNEIDER, Chairman

JOHN B. DRISCOLL, Commissioner

HOWARD L. ELLIS, Commissioner

CLYDE JARVIS, Commissioner

DANNY OBERG, Commissioner

ATTEST:

Madeline L. Cottrill
Commission Secretary

(SEAL)

NOTE: You may be entitle to a judicial review in this matter. If no Motion for Reconsideration is filed, judicial review may be obtained by filing a petition for review within thirty (30) days of the service of order. Section 2-4-702, MCA.